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Incongruity in Contemporary and Shari'ah Compliant Current Accounts and Ijārah Operated by Islamic Banking

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Abstract:
Current accounts and Ijārah has been foremost and important tools operated by the Islamic Financial Institutions. This study attempts to explore a few misgivings in the handling of current accounts by the Islamic banks in Pakistan. Financial management of Islamic banks is not under consideration which leads to the violation of Shari'ah's fundamentals. Also, in case of Ijārah, a bank's client suffers from financial losses which must be borne in Islamic Banking system. Islamic Banks transfer the burden of some charges emerging form ownership of leased asset on their clientele which does not have any justification according to Shari'ah. This research has been carried out by taking unstructured interviews from some of the concerned staff of Islamic Banks. The results depict that current accounts and Ijārah is in operation and need to be revised and refined and must comply with Shari'ah.

Key Words: *Ijārah, Current Accounts, Islamic Financial Institution, Financial Losses*

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1 Introduction:

The history of Islamic Banking industry in Pakistan is almost 25 years old. This industry is contributing lustrously in various segments of Pakistan's economy. The revival of Islamic banking sector in Pakistan in 2000 has been reported to be a giant Islamic banking industry in financial system of Pakistan. It is witnessing growth at a striking pace and has acquired approximately 10 percent of market share of the Pakistan's banking structure. Ijārah[1] is the trendiest mode of Islamic finance and banking, later than main financing share of Murābaha and Diminishing Mushārakah, 8.5% financing of Ijārah share has been stated of overall amount of financing during the year till June 2014[2].

At present, Pakistan economy is experiencing full fledge 5 (five) Islamic Banks, approximately 461 branches and sub branches of Islamic Banking of conventional banking are functioning as of June 30-2014 in Pakistan according to the Banking Policy & Regulations Department, State Bank of Pakistan.

Islamic Banking Industry is also supporting the economy by absorbing the human resource, mobilizing the money and application of funds in different economic and financial activities. Islamic Banks have introduced many financial products and services for the last many years and are still mustering their energy to come up with innovative style to capitalize their ideas under the experienced Shari'ah Advisory Board who further approves all the financial goods and services by keeping in view the Islamic jurisprudence. This Shari'ah Board is also responsible for the approved products and services being delivered by Islamic banks to check their Shari'ah compatibility. With the passage of time, Islamic Banks have been introducing a number of financial products and services to satisfy the consumer and industrial needs. These financial modes include some partnerships like Mushārakah, and Mudārabah,[3] Leasing mode (Ijārah) and also some trade modes like Murābaha[4], Musāwamah and Salam[5]. Islamic Banks' primary task is to mobilize the money by offering handsome deposits like Demand deposits and Time /Term deposits to serve the supply side of the money. The current accounts serve as a loan and it is considered as voluntary action on part of depositor because this account does not offer any profit on the deposited amount. The money under loan is used by the Islamic Banks for short term requirements.

Almost all Islamic Banks are mainly relying on Ijārah to meet medium term and long-term requirement of the economy in Pakistan. Ijārah is a transaction in which one party, institution or individual furnishes an asset to other party in question or individual against the specified rent. In fact, one party delegates the "rights of usufruct" to another party for a specified time period. Ijārah consists of two types, i.e. in one kind, individual or institution offers services to another (employee-employer relations) and/or offering some sort of corporal things (Lessor-lessee relations) to another on rent. Ijārah is like a Lease but there are some religious restrictions. The Islamic Banking recognizes the asset-based transactions whereas leasing is operated with money-based transaction, being a money-based transaction, a lessee does not return the asset to the original owner. Therefore, the Lease guided and directed by Shari'ah principles is called Ijārah[6] .To fulfill the

need of the sophisticated customers, all Islamic Banks have launched many kinds of Ijārah like Car Ijārah, House Ijārah etc.

Notwithstanding the facts, some of the Islamic banks still lag behind in delivering the products in accordance with Shari'ah principles. Surprisingly, some Islamic Banks are violating simple and similar basic conditions on the identical products which further creates ambiguities and cause decline of clientele rate in Islamic Banking Industry. It further leaves several confusions in the mind of people who really want to opt for interest free banking. This study will only focus on the Current accounts' management and practical implication of Ijārah operated by Islamic banks in Pakistan.

The main objective of the research is to review prevalent current accounts (some time termed as demand deposits and Ijārah) under the Shari'ah framework and to trace out the gaps and contradiction in practice of current account management and Ijārah in line with Shari'ah compatibility.

This is a qualitative research in nature and it also necessitates to gather already published theoretical and empirical literature and data. After reviewing the empirical and theoretical studies, current account and Ijārah and its issues will be explained in detail. To cover the practical implication of these two modes, some banking officials have been approached to gather information through unstructured interviews.

2. Scholarly Viewpoint Regarding Ijārah:

A number of Scholars have added to the above- mentioned subject with their own perspective.

1. Uthmānī[7] elucidated that "Muajjir" (Lessor) the eventual owner of asset has been given on lease agreement. The rental payment starts from the date when asset is delivered to "Mustajir" (Lessee). To avoid the intentional delay in the rental payments the lessee can be exposed to the financial fine. The amount collected in the context of the monitory penalty will be only used for welfare activities to avoid positive Ribā from the institution side[8].
2. Fatima[9] also explained a similar concept that financial penalty can be imposed but that should not be a share of institution's personal income otherwise it would lead to positive ribā.
3. Kamālī[10] highlighted the fact that simultaneously two contracts cannot be operated under the shadow of one contract. Sale or purchase agreement is entirely a different concept than the concept of Ijārah. In Ijārah, lessee may not have any intention to purchase the asset if and only if he only wants to enjoy the rights of usufructs.
4. The fact was explored the way Islamic banks pursue their functions and how they are operating Ijārah mode. The interesting findings of this study was that under the umbrella of Shari'ah commandments, the leasing and other mode sale/purchase dealings are exclusively two differing notions and these two should not be tangled/offered in one contract, as these two modes are self-determining and driven by separate set of rules[11].

5. The basic rules regarding Ijārah, are analogous to the rules of sale in some ways, as in both modes corporal asset in question is physically handed over to the second party for any personal and commercial consideration. The lone distinction lies between Ijārah and sale deal is that legal identity of the valuable property is offered to the customer when it comes to deal with sale, whereas, the legal status of the leased out asset continues to be under the ownership of eventual owner in Ijārah, but merely the rights of usufruct are transferred to lessee for the usage of asset[12].
6. The confusion generates regarding the rental payments in Ijārah, when one considers it as share of the total price. Abū Ghuddah investigated that if Ijārah contract is terminated at any point of time. Rental payments should be broken down into two parts: one concerning the rights of usufruct and an allocation of the price of asset. The second part should be repaid to the lessee at the termination of consent; otherwise it forms an unlawful earning of an individual or institution[13].

3. Current Accounts in Islamic Framework:

The current accounts refer to carrying no returns but sometimes it offers some benefits in the form of overdraft facilities, the current accounts and other deposits carrying no returns can be considered as Qarḍ or interest free loans from the depositors to the Islamic commercial banks (IIIE, 1997)[14]. It basically ensures safe pay- back of the principal amount to the depositors. Islamic commercial banks use these flow of funds into the productive projects and enjoys profit in return. The option of Amānah[15] and Wadī'a[16] will neither be viable nor feasible in line with handling the amount in current accounts. Amount in current account is considered as loan. Islam restricts creditors to their principal amount only. One cannot claim for above and excess to the principal amount. In the light of Quran, "All loans and financial liabilities must be matured on equal for equal basis" Al Baqarah 2:279:

فَإِنْ لَمْ تَفْعَلُوا فَأْذَنُوا بِحَرْبٍ مِنَ اللَّهِ وَرَسُولِهِ وَإِنْ تُبْتُمْ فَلَكُمْ رُءُوسُ أَمْوَالِكُمْ لَا تَظْلِمُونَ وَلَا تُظْلَمُونَ

But if you will not obey it, then there is a declaration of war from Allah and His messenger, and if you realize to leave Ribā then you will have right on your asset, neither creditor make debtor face loss nor creditor will face the loss.

Commercial banks can offer maximum suppleness in withdrawal of funds. Banks can also fix the period of lending and borrowing but that should be compatible to Shari'ah. Banks might offer overdraft facility to their depositors but on an interest free basis only.

4. Existing Current Accounts Handling by Islamic Banking:

The status of the pool of money deposited in current accounts is considered as loan by the Islamic Banks. The settlement of the money in current accounts should be exposed to be neither positive Ribā nor Negative Ribā. In reality, some of the Islamic Banks are charging against checque books and charges for ATM card fees as well. This exercise leads towards serious violation of Aḥkām on Ribā. As discussed above the Quranic verdict is very clear about lending and borrowing: "All loans and liabilities must be established on equivalent basis (in term of measuring unit of the object/item in question of the debt/loan)". Therefore, there is no justification for deducting the service charges in favor of cheque leaves and ATM cards. All the Islamic commercial banks may use this money in productive short-term investment opportunities to get profit and may recover all their borrowing cost. One of the foremost issues is always neglected in this context that Bank is not only providing its services to Bank rather Client is also providing its services to Bank as well. Therefore, lending charges should be borne by lender whereas cost emerging arising from borrowing that should be borne by borrowers to avoid negative Ribā. There is one other issue in the existing financial Islamic system that is the Bank also lets other banks to deduct Rs.15 from its current account holders in the binding of One-Link system. For Example if an account holder of Meezan Bank uses its ATM card to withdraw money from any other Bank either Islamic or Traditional, upon this transaction, a deduction of Rs. 15 is made. In fact, money in current account is a loan to the Meezan Bank and Meezan bank is bound to return the principal amount to the count of its bank clientele.

There is a violation in the dictum that "All loans and debts must be settled on equal basis (in term of measuring unit of the object in question of the loan/debt)". This fact can also be highlighted from the life of Holy Prophet SAW He said that verily Ribā was practiced in lending[17]. (Muslim, 2991). Ḥaḍrat Muhammad SAW also said that Indeed Ribā is in lending"[18]. (Muslim 2993).

5. Ijārah in Islamic Structure:

Uthmānī[19] (2000), Uthmānī[20] (2005) and Blueprints of Islamic Financial System[21], IIIE (1997) deliberately explained the basic rules concerning to Ijārah under the shadow of Islamic principles. These points are described below in the light of expert and scholarly judgment as mentioned above:

1. Ijārah is a business consent where the asset's owner only transfers the rights of usufruct to other party/ person/institution for an explicitly defined time period, as per the accord.
2. The leased item must be of valuable use. Thus, those items which do not have the feature of usufruct cannot be offered on Ijārah agreement.
3. It is indispensable for an applicable contract of lease that the ownership of asset under the Ijārah remains with the Lessor only, throughout the contract while the rights to use the asset are offered to the lessee. Another interesting characteristic of Ijārah contract is that those things which do not possess the quality of absorption/consumption do not come in Ijārah. For instance

lubricant money in the form of cash. The consumables like food, ammunition items etc. are not considered as they are perishable and cannot be returned.

4. In Ijārah, Lessor do not lose the ownership of the asset throughout the contract, therefore all the financial liabilities concerning the ownership should be paid by the eventual owner (Lessor) only, whereby the monetary liabilities associated with the utility of leased out asset shall be financed by the consumer/client.
5. Determination of time period of lease contract must be made in an explicit manner.
6. Once the purpose of hiring the asset has been mentioned in the contract, and then lessee does not have any ground to use that asset otherwise. If agreement is open in nature (without citing any particular use), lessee is absolutely free to utilize the subject of Ijārah. However, lessee can use the asset for any other purpose written in the Ijārah accord but with the approval of Lessor.
7. The lessee will be considered legally bound to recompense the Lessor losses for any impairment to asset of Ijārah as a result of maltreatment or laxity.
8. The factors which are not under control of lessee if any damage to leased asset takes place, all the compensation will be financed by the Lessor only. Thus an eventual owner of the asset retains the benefits till the maturity of Ijārah agreement. All the risk associated with leased items remain with the Lessor.
9. If one or more than two partners mutually own a leased item, income coming from the rental source shall be distributed between/among the partners in accordance with their proportion share in the capital of business.
10. An asset by the joint owners can be further leased out to his own share to his co-stakeholder only and not to any third party. Those assets which are not divisible cannot be leased out to other than co-partners.
11. It is mandatory for viable Ijārah consent that a leased asset be fully identified to both parties (Lessor and Lessee).
12. Determination of finally paid rentals for the whole contract is prerequisite for a valid Ijārah.
13. Different rent amounts may be fixed for different phases is permissible, subject to the provision that rent for each phase is agreed upon mutually and is explicitly described at the time Ijārah deal is made. If rent is fixed on the discretion of a Lessor only for any of the phase, Ijārah will be considered incompliant with Shari'ah Aḥkāmāt.
14. The Lessor cannot increase the rent at his own will only, rather that increase must be agreed upon by the two parties.

15. A Lessor can ask for an advance total amount of rent or a part of rental amount before offering the asset to tenant, but the advanced rental amount is accepted by owner and shall be thought as loan. This amount shall be counted towards final settlement between lessee and Lessor.
16. The time of lease agreement shall begin from the date when leased asset is delivered to the lessee, despite the consequences lessee has started to utilize the asset or not.
17. When the functions of asset given on Ijārah are lost for the rationale it was leased out, and repairing is impossible, the lease contract shall be considered terminated on the day when such loss was cropped up. However, if such loss is a result of any mishandling or carelessness on part of lessee, he will be accountable to recompense the depreciated value of the asset as before the loss to Lessor.

All Islamic Banks are following the same structure as discussed above regarding Ijārah when an offer of Lease mode to their clients is made. Having been reviewed the idealistic approach towards Ijārah; one can adequately investigate the current practice of the financial institution. As for as conventional banking approach of Ijārah is concerned which does not have any grounds in Islam. Structural interviews were conducted from the Islamic Banks. The criticism in current Ijārah is presented on the basis of perception of management of the Islamic financial institution.

6. Existing Ijārah Operated by the Islamic Banks:

Currently, many banks depend on the Ijārah mode. More than 80% of the bank transactions are followed by the Ijārah operations. In recent few years, Ijārah has carried high fame among all the Islamic financial institution in Pakistan.

In current scenario, the Islamic Banks charge all documentation charges from the client in the capacity of Lessee. In the context of Car Ijārah, the Bank serves as a Lessor while the client presents the lessee status. All charges up-and-coming from ownership must be taken into account by Lessor. These charges include ownership cost, fees for number etc. Theoretically speaking, this is ownership cost which a Lessor must pay. In practice, all the charges are transferred to Lessee whereas he does not have anything to do with ownership.

According to guidelines of State Bank of Pakistan, every product financed and leased by the commercial banks must be insured. Following this paradigm, all Islamic Commercial Banks are providing risk coverage associated with the assets. In the context of Ijārah, Islamic Bank first purchases the asset, gets the ownership along with constructive possession. So after getting the ownership, it leases the asset out to the lessee. One questionable thing in this operation is that Lessee has to bear all the cost emerging from risk coverage, despite that fact Islamic Bank is sole owner of the asset. Secondly, many Islamic Scholars have highlighted that if accidents do not happen and Islamic Banks hold that pool of money accrued in car insurance is not given back to the Policy holder, then the withheld amount does not have any justification in Islamic Framework. This negative activity has been

termed as confiscation by the Islamic Scholars. Islamic banks are found silent on these issues. Ultimately, these issues enhance the financial burden of the lessee.

Concerning to the depreciation, Islamic Banks do not have any knowledge and rule in the depreciation in the context of car leasing. They are of the view that the assets which they are using in Ijārah are not subject to depreciation rather they appreciate any clients who take this benefit. So the Islamic Banks do not have any strategy.

Recently, some banks have made it obligatory that after the termination of Ijārah contract, lessee has to purchase the asset at the end. Primarily, it was an optional decision if a bank client is not willing to hold that car, he can return the asset to Lessor and could get his security back. Now, it has been designed as compulsory to purchase at the end of the Ijārah contract whereas, conditional sale is not permitted by Islam.

7. Conclusion:

Current accounts are not being managed according to the main principles of Islam. In lending and borrowing transaction, there is clear cut stance that all loans and debts must be settled down on equal for equal basis. But deduction of some charges on interest free lending leads to ribawī (interest bearing) dealing. All the lending cost should be financed by the Lender and all the borrowing cost should be borne by the borrowers. The way, Islamic Banks are operating the Ijārah, it contradicts some of the basic rules of Ijārah. Various costs which emerge from the ownership is transferred to lessee whereas this cost should be borne by Lessor. In Ijārah, only right of usufructs is transferred, not the right of ownership. The Islamic Banks are focusing on the economic rationale rather than on Islamic Paradigm. Finally as an Islamic Republic, Pakistan is one of the main responsibilities of state to design and formulate interest free economic and financial institutions. Government should ensure the Shari'ah compatibility of all financial products and services at Islamic Bank level with the help of Islamic Branch of State Bank of Pakistan.

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1 Ijārah is an Arabic terminology used for Leasing, is defined as rights of usage given to the user of an asset for a specific time period against monetary reward (Rent).

2 State Bank of Pakistan, Islamic Bank Bulletin-June 2014 abbreviated as (SPB-IBB-June 2014).

3 Mushārakah and Mudārabah are partnerships mode, former characterizes as contribution on capital from all partners and all or few can participate in decision making whereas later postulates one partner contributes in capital and second partner only manage the business.

4 It is one of the Islamic trade modes, described as sale on differed payment.

5 It is also one of the sale modes in Islam, delivery of asset is referred to future and full advance payment is made at the time of deal.

6 Uthmānī, 2010

7 Muftī Taqī Uthmānī, is retired Justice and currently running Religious Institute Dār Ul Ulūm in Karachi.

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15 Amānah is simply safe keeping where ownership remains with the ultimate owner and second party cannot use the asset in question.

16 Wadī'a is used where natural growth can be observed like in animals. In wadī'a, ownership is not lost, but second party can use the asset.

17 Muslim, 2991

18 Muslim 2993

19 Muftī Taqī Uthmānī is retired Justice of Pakistan and currently running a Dār ul Ulūm in Karachi.

20 Muftī Zubair Uthmānī, Shari'ah Advisor, Muslim Commercial Bank Ltd.